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No. 905

In the Supreme Court of the United States

OCTOBER TERM, 1959

SECURITIES AND EXCHANGE COMMISSION, PETITIONER

v.

LEA FABRICS, INC., ET AL.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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JURISDICTION

The order of the Court of Appeals (App., *infra*, pp. 18–19), affirming the judgment of the district court, was entered on December 8, 1959, and a timely petition for rehearing was denied on January 5, 1960 (App., *infra*, p. 19). On March 31, 1960, Mr. Justice Brennan extended the time for filing a petition for a writ of certiorari to and including May 4, 1960. The order of the Court of Appeals denying the Commission's motion to vacate the judgment for mootness was entered on March 23, 1960 (App., *infra*, p. 20). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the Court of Appeals should have vacated its prior judgment affirming an order of the district court, sustaining the propriety of proceeding under Chapter XI of the Bankruptcy Act, when the order of the district court had been rendered moot by an adjudication of bankruptcy.

STATUTE INVOLVED

Chapters X and XI of the Bankruptcy Act, 52 Stat. 883 and 905, 66 Stat. 431 (11 U.S.C. 501, *et seq.* and 701, *et seq.*) are involved in this proceeding substantially in their entirety.

STATEMENT

The debtor, Lea Fabrics, Inc., filed a petition for an arrangement under Chapter XI of the Bankruptcy Act on January 21, 1959. It has outstanding over 1,000,000 shares of $5 par value common stock held by approximately 1,000 persons. According to the debtor's schedules, as of March 3, 1959, its assets

were $1,620,500 and liabilities were $1,752,785. The assets consisted of plant, machinery and equipment, certain television properties and stock in other companies. All of these were mortgaged or pledged. The debtor had been in business for many years manufacturing automobile fabrics. Several years prior to the filing of the petition, however, its business was materially altered by a new management to the point where the debtor no longer engaged in manufacturing operations. Instead, it sold its inventory and, partly through the issuance of newly-authorized shares of stock and the mortgaging or pledging of its theretofore lien-free assets, the debtor acquired new assets, including motion picture and television rights (which subsequently were sold, pledged or transferred by the debtor in exchange for stock of a television film corporation) and three steamships (two of which were placed in a newly-formed subsidiary of the debtor and later exchanged for stock in a third corporation). Many of these transactions involved companies that were under common control with the debtor. These transactions resulted in over-all losses to the debtor (R. 16a–19a, 79a, 83a–84a).

The debtor's plan of arrangement provided for the payment in full of priority claims and administration expenses and for a twenty-percent payment to unsecured creditors in full satisfaction of their claims (R. 20a). This arrangement was accepted on March 24, 1959 (R. 20a); confirmation was postponed from time to time at the debtor's request, until September 23, 1959, in order to enable it to work out necessary

agreements with outside interests which would presumably permit the debtor's substantial operating losses to be utilized for federal income tax savings (R. 51a–56a, 57a–63a, 66a–69a, 70a–73a, 74a–76a). In the meantime, the realty and chattel mortgages on the debtor's property were foreclosed and sold. Shortly before September 23, 1959, the debtor had worked out a series of proposed transactions which included (1) the borrowing of the necessary cash for the Chapter XI arrangement from a company associated with the present management, which would receive debtor's notes or other evidences of indebtedness, (2) the debtor's recapitalization through issuance of new preferred stock and a reduction to one-fourth of the amount of common stock outstanding; (3) the acquisition of new assets with preferred and common stock thus made available, (4) the sale of these assets for cash, (5) with cash so obtained and with stock, the purchase of the assets of a partnership engaged in the financing business, (6) payment of most of the advances for the Chapter XI arrangement, and (7) the debtor's entry into the financing business (R. 20a–22a).

On September 23, 1959, the Securities and Exchange Commission, pursuant to Section 328 of Chapter XI, 11 U.S.C. 728, moved to intervene and to dismiss the Chapter XI proceeding unless the debtor's petition was amended to comply with the requirements of Chapter X (R. 8a–14a). In its motion and allied papers, the Commission contended that the Chapter XI proceeding should be dismissed because the arrangement was but a single step in a pervasive

reorganization, which those in control of the debtor were seeking to implement beyond the Chapter XI court's jurisdiction and for which the provisions of Chapter X were more appropriate (R. 10a, 13a, 20a–22a). The district court denied the Commission's motion (R. 35a–43a), and on appeal by the Commission the Court of Appeals affirmed (App., *infra*, pp. 13–19); it subsequently denied a petition for rehearing (App., *infra*, p. 19).

Pending review in the Court of Appeals the proceeding in the district court had been stayed. Thereafter, the debtor again sought adjournments in the district court; but, on February 17, 1960, the debtor was unable to provide a $5,000 indemnity required by the district court as a condition for a further adjournment pursuant to Section 326 of Chapter XI, 11 U.S.C. 726. On February 18 (after denial of rehearing by the Court of Appeals), the district court, having found that payment of such indemnity was not forthcoming and that "the possibilities of the debtor raising the money to effectuate its proposed plan of arrangement did not seem possible or probable at this time," adjudicated the debtor a bankrupt pursuant to Section 327 of the Bankruptcy Act, 11 U.S.C. 727, and ordered that bankruptcy be proceeded with.

Thereupon, the Commission moved that the Court of Appeals vacate its judgment of December 8, 1959, recall its mandate to the district court, if deemed necessary, and remand to the district court with directions to that court to vacate as moot its order refusing to dismiss the debtor's petition under Chapter XI.

This motion was denied, without opinion, by the Court of Appeals on March 23, 1960 (App., *infra*, p. 20).

REASONS FOR GRANTING THE WRIT

Upon the debtor's adjudication as a bankrupt prior to the expiration of the statutory period for judicial review,[2] the decision of the Court of Appeals upholding the propriety of the debtor's resort to Chapter XI, as against Chapter X, of the Bankruptcy Act was rendered moot and the debtor's proposed Chapter XI arrangement became a nullity.

Under similar circumstances this Court in the past has granted certiorari to reverse or vacate a judgment below and has remanded with directions to dismiss the action. For example, in *Federal Power Commission* v. *Midwestern Gas Transmission Company*, 358 U.S. 280, the decision of the court of appeals was vacated on the ground of mootness, since the issue involved (the necessity for consolidation of hearings before the Power Commission) had become moot by reason of an amendment to the application of one of the companies seeking consolidation prior to the expiration of the time for filing a petition for

[2] The debtor was adjudicated a bankrupt on February 18, 1960. The date of the denial of the petition for rehearing by the Court of Appeals, January 5, 1960, started the running of the ninety-day period during which a petition for a writ of certiorari could be filed and, accordingly, that period would not expire until April 4, 1960. 28 U.S.C. 2101(c), *Pfister* v. *Northern Illinois Finance Corp.*, 317 U.S. 144, 149–150. That period has since been extended. See p. 2, *supra*.

a writ of certiorari in this Court. And see *Brownlow v. Schwartz*, 261 U.S. 216, where this Court reversed and vacated the judgment of the court of appeals since its determination as to the propriety of a refusal to issue a building permit had been rendered moot by virtue of the issuance of the permit subsequent to the decision of the court of appeals but prior to the filing of a writ of error. Similarly, in *American Public Power Association* v. *Power Authority*, 355 U.S. 64, this Court vacated the decision of the court below where the question of the power of the Federal Power Commission to issue a license to the New York Power Authority was rendered moot by virtue of the enactment by Congress of legislation authorizing and directing issuance of the license during the period provided by statute for filing a petition for a writ of certiorari. See also, for example, *United States* v. *Alaska Steamship Co.*, 253 U.S. 113; *Leader* v. *Apex Hosiery Co.*, 302 U.S. 656; *Sawyer* v. *Dollar*, 344 U.S. 806; *Garcia* v. *Lanton*, 348 U.S. 856; and *McKay* v. *Clackamas County*, 349 U.S. 909. Cf. *First Union Trust & Savings Bank* v. *Consumers Company*, 290 U.S. 585, where the issue of the propriety of the district court's granting an injunction against foreclosure upon certain property was rendered moot pending appeal to the Court of Appeals because the district court had lost jurisdiction over the property as a result of the debtor's subsequent adjudication as a bankrupt; this Court reversed the

affirmance by the Court of Appeals with directions that the injunction order be vacated.

These decisions are consistent with a long established policy respecting intervening mootness. As this Court has stated: "Where it appears upon appeal that the controversy has become entirely moot, it is the duty of the appellate court to set aside the decree below and to remand the cause with directions to dismiss." *Duke Power Company* v. *Greenwood County,* 299 U.S. 259. Thus, to prevent abstract determinations from governing results of subsequent cases, this Court has reversed and vacated a lower court judgment, whether or not there are plausible grounds for predicting that the issue rendered moot might become justiciable in the future. See *United States* v. *Hamberg-American Company,* 239 U.S. 466, 475; *Commercial Cable Company* v. *Burleson,* 250 U.S. 360; *Leader* v. *Apex Hosiery Co.,* 302 U.S. 656, *supra.* The vacation of the judgment of the lower court where the case has become moot during the course of appellate review will "prevent a judgment, unreviewable because of mootness, from spawning any legal consequences." *United States* v. *Munsingwear,* 340 U.S. 36, 41. It does not deprive the parties of whatever rights might accrue to them in the future; on the contrary, it "* * * clears the path for future relitigation of the issues between the parties and eliminates a judgment, review of which was pre-

vented through happenstance." *Id.* at 40.[3] In that case the failure of the plaintiff to move for vacation of the district court's order on the ground of mootness was held to preclude it from challenging the holding in a subsequent proceeding between the parties.

In the present case, the determination of the court below, if not vacated, may well affect the result of other cases under Chapter XI of the Bankruptcy Act. The Commission argued in both lower courts that the proposed arrangement under Chapter XI was improper in view of the necessity for a pervasive reorganization of the debtor involving both a material readjustment of its capital structure and its entering into a new field of business. This latter step was necessary because all assets of consequence, except a tax loss carry-forward, had been lost through foreclosure.

The debtor intended to effectuate these necessary steps outside the jurisdiction of the district court by private unsupervised arrangements, thus accomplishing a reorganization in part by an arrangement in

[3] See Scott, *Collateral Estoppel by Judgment*, 56 Harv. L. Rev. 1, 16 (1942): "In situations * * * where the controversy has become moot before the appellate court has made its decision, it would seem that the better practice is not merely to dismiss the appeal, but to dismiss the suit or to direct the lower court to do so. The result then clearly is that the matter will not be *res judicata*, since there is no judgment on the merits."

court under Chapter XI and in part by corporate action out of court. The Commission argued that this was comparable to the dual-phased plan of reorganization proposed in *Securities and Exchange Commission* v. *United States Realty & Improvement Company*, 310 U.S. 434, where this Court held it reversible error to resort to Chapter XI instead of Chapter X. Cf. *General Stores Corporation* v. *Shlensky*, 350 U.S. 462. The Commission also contended that, if rehabilitation could be accomplished at all within the framework of the Bankruptcy Act, resort should have been had to Chapter X because of its broader remedial scope and greater protective features and the needs to be served.

Had the case not become moot, the correctness of the ruling of the court of appeals could have been submitted to this Court for review. However, the intervening bankruptcy of the debtor has made the order sustaining Chapter XI proceedings moot so that review of the merits here is now precluded. Nevertheless, the court below has refused to vacate its judgment approving the order, so that that judgment now stands as a precedent for what the Commission believes to be an erroneous use of Chapter XI as against Chapter X of the Bankruptcy Act.[4]

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[4] It is possible that prior to the conclusion of the pending bankruptcy proceedings a new petition for an arrangement under Chapter XI may be filed, since, under Section 321 of that chapter, 11 U.S.C. 721, such a petition may be filed "either before or after * * * adjudication." If this happened while the court of appeals judgment remains outstanding, it might be urged that, under the doctrine of the *Munsingwear* case, the Commission would be precluded from contesting the use of Chapter XI by this debtor.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted, the judgment of the court below should be vacated and the cause should be remanded to the district court with directions that it vacate its order denying petitioner's motion to dismiss the Chapter XI proceeding.

Respectfully submitted.

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MAY 1960.

APPENDIX

United States Court of Appeals for the Third Circuit

No. 13054

IN THE MATTER OF LEA FABRICS, INC., DEBTOR

SECURITIES AND EXCHANGE COMMISSION, APPELLANT

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY

Argued November 17, 1959

Before BIGGS, *Chief Judge,* and GOODRICH and McLAUGHLIN, *Circuit Judges*

Opinion of the Court

(Filed December 8, 1959)

By GOODRICH, *Circuit Judge.*

This is an appeal from a judgment of the District Court for New Jersey denying a motion of the Securities and Exchange Commission to dismiss a Chapter XI bankruptcy proceeding unless the petition therein be amended to comply with the requirements of Chapter X. The district judge filed no written opinion but this Court has had the benefit of reading his oral opinion issued prior to the order denying the motion. The Securities and Exchange Commission takes this appeal.

The debtor, Lea Fabrics, Inc., formerly manufactured "a special and unique type of carpeting de-

signed and fabricated to serve the automobile trade." This business fell off and became a losing venture. The corporation then interested itself in various other enterprises the nature of which is not necessary to detail here. Its real and movable property was mortgaged and those mortgages have been foreclosed, the foreclosures resulting in the creation of deficiencies. The debtor is insolvent. On November 10, 1958, on petition of a creditor, a statutory receiver was appointed by the Chancery Division of the Superior Court of New Jersey, Essex County. This receivership continued for about two months and was terminated when the debtor filed a petition for an arrangement under Chapter XI of the Bankruptcy Act. 11 U.S.C.A. §§ 701–99. The receiver appointed in the Chapter XI proceeding was the same person who had served as receiver in the prior state court proceedings.

After several months an arrangement was proposed and agreed to by the necessary majority of the creditors. Under this arrangement the unsecured creditors are to receive twenty cents on the dollar. There is to be a sufficient fund ($300,000) to be available for this purpose obtained by management on an unsecured loan. This fund will pay the expenses of administration in full, the priority claims in full and the general creditors twenty cents on the dollar as indicated. After the plan was proposed the settlement of the matter was delayed from time to time while management sought to find the money necessary to consummate the arrangement. At the hearing where confirmation was to be sought the Securities and Exchange Commission intervened[1] and made its motion

[1] SEC intervention was predicated on Section 328 of the Bankruptcy Act, added in 1952, 11 U.S.C.A. § 728 (Supp. 1958), which in pertinent part reads as follows:

"§ 728. Dismissal, proceedings; amended petition

"The judge may, upon application of the Securities and Ex-

to dismiss the Chapter XI proceeding unless the debtor would amend so as to come in under Chapter X. This the debtor refused to do.

All of the decisions to which we have been referred, five in number, dealing with the problem of whether to dismiss Chapter XI proceedings unless the debtor brings itself under Chapter X place great emphasis upon the discretion vested in the trial judge on this question. The cases are as follows: *SEC v. United States Realty Co.*, 310 U.S. 434 (1940); *In re Transvision, Inc.*, 217 F. 2d 243 (2d Cir. 1954), *cert. denied* 348 U.S. 952 (1955); *General Stores Corp.* v. *Shlensky*, 350 U.S. 462 (1956); *SEC* v. *Wilcox-Gay Corp.*, 231 F. 2d 859 (6th Cir. 1956); *SEC* v. *Liberty Baking Corp.*, 240 F. 2d 511 (2d Cir.), *cert. denied* 353 U.S. 930 (1957).[2]

That discretion, it is to be observed, is not one limited greatly by settled legal rules. True, it has been categorically stated that Chapter XI is not solely for small corporations and Chapter X not solely for big corporations. *General Stores Corp.* v. *Shlensky*, 350

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change Commission * * * if he finds that the proceedings should have been brought under chapter 10 of this title, enter an order dismissing the proceedings under this chapter, unless, within such time as the judge shall fix, the petition be amended to comply with the requirement of chapter 10 of this title for the filing of a debtor's petition or a creditors' petition under such chapter, be filed * * *."

[2] For a review of the uncertain legislative history and the cases prior to the Supreme Court's affirmance in *General Stores*, the Sixth Circuit's affirmance in *Wilcox-Gay* and the Second Circuit's reversal in *Liberty Baking*, see: Weintraub, Levin & Novick, *Chapter X or Chapter XI: Coexistence for the Middle-Sized Corporation*, 24 Fordham L. Rev. 616 (1956).

For the story thereafter see: Weintraub & Levin, *A Sequel to Chapter X or Chapter XI: Coexistence for the Middle-Sized Corporation*, 26 Fordham L. Rev. 292 (1957).

U.S. 462, 465–66 (1956). But the criterion by which the district judge's discretion is to be exercised has to do with the best arrangement for all parties concerned under the circumstances confronting the particular corporation. *Ibid.*

The discretion was properly exercised in this instance. The debtor's corporate structure is a simple one; it has common shareholders but no preferred shareholders or bondholders. Management owns or controls more than half the common stock. The proposed arrangement does not interfere in any way with whatever rights shareholders may have. The plan has been agreed to by the unsecured creditors and the priority creditors, including tax claimants, are fully cared for.

Not the least of the considerations which prompt approval of the trial judge's exercise of discretion is the situation of this corporation. It was engaged, apparently profitably, in the manufacture of goods no longer in market demand. Its other ventures have been unsuccessful. It has no tangible assets except some television properties the value of which is speculative. According to the record, all the corporation now has of any substantial value is a tax loss carry-over.

Chapter X proceedings would involve the appointment of a disinterested trustee and investigation into the previous operation of this corporation before a plan for rehabilitation could be submitted, if indeed such a plan ever could be worked out. All of this necessarily involves time and money. There is $33,000 under the control of the referee which he insisted on being deposited as a condition to granting continuances while funds were being sought to effect the plan. The Securities and Exchange Commission says that "presumably" this $33,000 would be avail-

able for Chapter X expenses. We do not see the basis on which the presumption rests, nor are we advised how far the $33,000 would go in providing for the expenses of such investigation and report as a trustee might make. The $300,000 to be used to pay creditors, as we understand it, is not yet cash in hand but will be upon approval of the Chapter XI plan if it is not too long delayed.

There is, in this case, a situation where, as Judge Medina said in the *Transvision* case, "there may be some basis for suspecting possible improprieties in past management." 217 F. 2d at 247. What we say here is by no means to be interpreted as giving past management of Lea Fabrics a health certificate. The point is that we do not know whether there is basis for anything more than "possible improprieties." If there is, the arrangement here does not deprive any shareholder of his rights to enforce claims for losses occasioned by improper management. To further quote from Judge Medina's opinion:

> Certainly, so ephemeral a suspicion is not an adequate basis upon which to overturn a plan which the District Court, on the facts before it at this time, appears to believe may ultimately be found feasible, and one which, necessarily, would have to be acceptable to at least a majority of the unsecured creditors before being approved. *Ibid.*

While the New Jersey receivership was in progress the receiver made a seven-day investigation of the debtor's relations with certain other companies in which management was also interested. There was not, at the time, even enough money to have the testimony transcribed. The investigation developed noth-

ing of value. It was admittedly a nonthorough one but in a week's hearing it should have produced at least some clues if clues were to be found.

The court here was confronted with the expensive possibility of an investigation to determine whether vague suspicions were well founded. The debtor has no assets with which to finance such an investigation. Even if a plan evolved under Chapter X which was "fair and equitable," 11 U.S.C.A. § 621(2), the shareholders would stand little chance of profiting by it. We think that the district court exercised sound business, as well as legal, judgment in denying the motion to dismiss the Chapter XI proceeding.

The judgment of the district court is affirmed.

United States Court of Appeals for the Third Circuit

No. 13054

IN THE MATTER OF LEA FABRICS, INC., DEBTOR

SECURITIES AND EXCHANGE COMMISSION, APPELLANT

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY

Present: BIGGS, *Chief Judge,* and GOODRICH and MCLAUGHLIN, *Circuit Judges.*

Judgment

This cause came on to be heard on the record from the United States District Court for the District of New Jersey and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the

said District Court in this case be, and the same is hereby affirmed.

Attest:

IDA O. CRESKOFF, *Clerk.*

DECEMBER 8, 1959.

United States Court of Appeals for the Third Circuit

No. 13054

IN THE MATTER OF LEA FABRICS, INC., DEBTOR

SECURITY AND EXCHANGE COMMISSION, APPELLANT

SUR PETITION FOR REHEARING

Present: BIGGS, *Chief Judge,* and GOODRICH, MCLAUGHLIN and FORMAN, *Circuit Judges.*

After due consideration the petition for rehearing in the above-entitled case is hereby denied.

By the Court:

GOODRICH,
Circuit Judge.

Dated: January 5, 1960.

United States Court of Appeals for the Third Circuit

No. 13054

IN THE MATTER OF LEA FABRICS, INC., DEBTOR

SECURITIES AND EXCHANGE COMMISSION, APPELLANT

Present: BIGGS, *Chief Judge*, and GOODRICH and MCLAUGHLIN, *Circuit Judges*.

Upon consideration of the motion by Securities and Exchange Commission to vacate the opinion and judgment in the above case for mootness;

It is ordered, That the motion be, and it is hereby denied.

By the Court:

GOODRICH,
Circuit Judge.

MARCH 23, 1960.

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IN THE

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OCTOBER TERM, 1959.

No. 905.

SECURITIES AND EXCHANGE COMMISSION,

Petitioner,

v.

LEA FABRICS, INC., *et al.*,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF OF RESPONDENTS, LEA FABRICS, INC., DEBTOR, UNSECURED CREDITORS' COMMITTEE AND RECEIVER OF DEBTOR OPPOSING CERTIORARI.

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IN THE

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SECURITIES AND EXCHANGE COMMISSION,

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BRIEF OF RESPONDENTS, LEA FABRICS, INC., DEBTOR, UNSECURED CREDITORS' COMMITTEE, AND RECEIVER OF DEBTOR, OPPOSING CERTIORARI.

Jurisdiction.

The Order of the United States Court of Appeals for the Third Circuit sought to be reviewed was entered on March 23, 1960 (App. annexed to petition p. 20). The jurisdiction of this Court is invoked under 28 U. S. C. 1254(1).

Opinions Below.

The United States Court of Appeals for the Third Circuit filed no opinion in connection with its order of March 23, 1960 denying petitioner's motion to vacate on the ground of mootness its earlier judgment affirming the order of

the District Court. The opinion of the Court of Appeals upholding the order of the District Court on the merits is reported in 272 F. 2d 769, and is set forth at pages 13-18 of appendix to petition. The oral opinion of the District Court is not reported, but is set forth in petitioner's appendix to its brief in the Court of Appeals (35a-43a).[1]

Question Presented.

Whether the United States Court of Appeals for the Third Circuit properly refused to vacate its opinion and judgment affirming an order of the District Court sustaining the propriety of a proceeding under Chapter XI of the Bankruptcy Act after the entry by the District Court of an adjudication in bankruptcy.

Statute Involved.

11 U. S. C. 728 (Section 328 of the Bankruptcy Act):

> "The judge may, upon application of the Securities and Exchange Commission or any party in interest, and upon such notice to the debtor, to the Securities and Exchange Commission, and to such other persons as the judge may direct, if he finds that the proceedings should have been brought under chapter 10 of this title, enter an order dismissing the proceedings under this chapter, unless, within such time as the judge shall fix, the petition be amended to comply with the requirement of chapter 10 of this title for the filing of a debtor's petition or a creditors' petition, under such chapter, be filed. Upon the filing of such amended petition, or of such creditors' petition, and the payment of such additional fees as may be required to comply with section 532 of this title, such amended petition or creditors' petition shall

[1] Numerals followed by the letter "a" refer to the appendix of the proceedings in the United States Court of Appeals for the Third Circuit.

thereafter, for all purposes of chapter 10 of this title, be deemed to have been originally filed under such chapter."

Statement.

The debtor, a Delaware corporation, all of whose visible assets and whose principal place of business were in the City of Newark, County of Essex, and State of New Jersey, on January 21, 1959 filed a proceeding for an arrangement under Chapter XI of the Bankruptcy Act (24a). Prior to that, on July 7, 1958, a creditor of the debtor had filed a complaint in the Chancery Division of the Superior Court of New Jersey seeking the appointment of a receiver for the debtor under the insolvency provisions of the Corporation Act of the State of New Jersey. On November 10, 1958 the Superior Court of New Jersey adjudged the debtor corporation insolvent within the meaning of the Statutes of the State of New Jersey, R. S. 14:14-3, and appointed a Statutory Receiver pursuant to the said Statute for the assets and affairs of the debtor corporation (24a).

The debtor proposed a plan of arrangement in the Chapter XI proceeding, which was approved by its creditors (25a). In essence the plan provided for (a) payment of all priority claims in full, (b) payment of all administration expenses in full, and (c) payment to all general unsecured creditors of 20% of their claims as finally approved and allowed.

On September 23, 1959, the Securities and Exchange Commission (S. E. C.), pursuant to Section 328 of Chapter XI, 11 U. S. C. 728, moved to intervene and to dismiss the Chapter XI proceeding unless the debtor's petition was amended to comply with the requirements of Chapter X (8a-14a).

When the debtor and its counsel, the Receiver, the attorney for the Receiver, and the attorney for the Creditors' Committee arrived in Court a few minutes before two o'clock on September 23, 1959, the date and time set by the Referee for the hearing on the confirmation of the plan of arrangement proposed by the debtor and approved by creditors, they were met by the attorneys for the S. E. C. These attorneys announced that at one o'clock in the afternoon, an hour before the hearing on the confirmation of the plan, they had filed with the Clerk of the United States District Court for the District of New Jersey a motion for intervention, and had applied for an order to show cause under Section 328 of the Bankruptcy Act (26a). The hearing before the Referee was immediately adjourned. All counsel thereupon appeared before Judge Wortendyke, Judge of the United States District Court on the motion of the S. E. C. (26a). All parties agreed that the motion to intervene should be granted at once and the debtor, the attorney for the Receiver, and the attorney for the Creditors' Committee urged that a prompt hearing on the order to show cause be had, because of the large sum of money that was tied up and that there was reason to believe that the money might not be available if any lengthy litigation over the motion of the S. E. C. ensued.

Judge Wortendyke set the hearing down and on October 2, 1959 heard the matter for almost the entire day. At the conclusion of the hearing he denied the application of the S. E. C. under Section 328 of the Bankruptcy Act, and discharged the order to show cause which he had granted. An order to that effect was entered on October 14, 1959 (42a), from which order an appeal was taken by the S. E. C. to the United States Court of Appeals for the Third Circuit. The order was affirmed by that Court on December 8, 1959. It is this judgment which the S. E. C. now asks to have vacated.

Thereafter the S. E. C. filed its petition for rehearing. An answer to the petition for rehearing was filed by the respondents herein (App. *infra*, pp. A-1 to 4). On January 5, 1960 the Court denied the motion and the mandate of the Court was then issued on January 11, 1960. An order on the mandate was then issued. No application for a writ of certiorari was filed by the S. E. C. to review the order of the Third Circuit Court of Appeals entered on December 8, 1959 affirming the order of the District Court.

At the hearing before the Referee on confirmation of the plan on September 23, 1959, and subsequently before Judge Wortendyke on October 2, 1959, the debtor stated that the cash necessary to consummate the plan of arrangement was available (26a).

In an affidavit of Fred S. Payne, filed with Judge Wortendyke in opposition to the motion of the S. E. C. he stated, as President of the debtor corporation:

> *"The cash necessary to pay creditors' claims is being advanced to the Debtor without any security or strings whatsoever. On confirmation of the Chapter XI Plan, therefore, the Debtor's capital structure will remain absolutely simple and unchanged. Neither the rights of creditors nor stockholders will be impaired.* (Italics supplied.)
>
> "Said Plan bears no relationship to and is not dependent on management's proposals and plans for the Debtor's future, as suggested by the Commission" (32a).

Judge Goodrich, in his opinion sustaining the order of the District Court, stated:

> "After several months an arrangement was proposed and agreed to by the necessary majority of the creditors. Under this arrangement the unsecured creditors are to receive twenty cents on the dollar.

There is to be a sufficient fund ($300,000). to be available for this purpose obtained by management on an unsecured loan." (App. annexed to petition, p. 14.) (Italics supplied.)

The arrangements of the debtor outlined by the S. E. C. at page 4 of its petition herein were not the arrangements through which the debtor proposed to effectuate its plan of arrangement. The debtor's arrangements to effectuate its plan of arrangement were to borrow $300,000.00 on an unsecured basis with no strings attached, as outlined by Mr. Payne in his affidavit, *supra*, and as found by Judge Goodrich in his opinion, *supra*.

At a hearing before the Honorable William H. Tallyn, Referee in Bankruptcy, before whom the Chapter XI proceeding was pending, held on February 5, 1960, it was disclosed by the attorney for the debtor in a colloquy before the Referee, that the debtor was having difficulty in raising the funds necessary to effectuate the plan of the debtor and thus secure confirmation of such plan by the Court. In testimony given at the same hearing Mr. Fassoulis, who was the controlling stockholder of Financial Consultants, which was the largest stockholder of the debtor, in addition to being the financial advisor of the debtor, stated that prior to the S. E. C. motion the debtor had had a firm commitment for $300,000.00 to effectuate the plan, which had been lost during the period of the S. E. C. litigation (App. *infra*, p. 5).

On February 18, 1960, when it was obvious that funds needed to confirm the plan were no longer available, the Referee entered an order adjudging the debtor a bankrupt and ordered that bankruptcy be proceeded with.

ARGUMENT.

POINT I.

The decision of the court below refusing to vacate its opinion and judgment was correct.

A. This petition of the S. E. C. for certiorari seeks to review an order of the Court of Appeals properly entered by that Court.

It must be clearly kept in mind at all times that the S. E. C. seeks a review in this Court of the order of the United States Court of Appeals for the Third Circuit entered March 23, 1960, denying the motion of the S. E. C. to vacate its opinion and order entered on December 8, 1959, affirming the decision of the District Court. No review of this latter order is sought here. The S. E. C. did not file any petition for certiorari to review said order.

Instead, the S. E. C. chose to file a petition with the Court of Appeals asking it to vacate its opinion and judgment on the ground that the case had become moot, because on February 18, 1960 the Referee in Bankruptcy had decided that the debtor should be adjudicated a bankrupt. Prior to this petition of the S. E. C. the Court of Appeals had issued its mandate on January 11, 1960. Thereafter the District Court entered its order on the mandate on January 12, 1960. We submit that the Court of Appeals in entering its order of March 23, 1960 exercised sound discretion in refusing to recall its mandate and vacate its opinion and judgment.

No possible question of mootness existed at the time the Court of Appeals handed down its opinion and rendered its judgment.

B. The cases cited by the S. E. C. lend no support to its petition for a writ of certiorari.

All of the cases cited by and relied upon by the S. E. C. in its petition here were called to the attention of the Court of Appeals by the S. E. C. in its brief before that Court upon its motion to vacate the decision and judgment of that Court. A careful analysis of these cases shows that they lend no support to the petition of the S. E. C.

One of such cases relied upon by the S. E. C. is *United States* v. *Munsingwear*, 340 U. S. 36, at pp. 39 and 40, 95 L. Ed. 36. Justice Douglas, speaking for this Court, at page 39 said:

> "The established practice of the Court in dealing with a civil case from a court in the federal system which has become moot while on its way here or pending our decision on the merits is to reverse or vacate the judgment below and remand with a direction to dismiss. That was said in Duke Power Co. *v.* Greenwood County, 299 U. S. 259, 267, 81 L. Ed. 178, 182, 57 S. Ct. 202, to be 'the duty of the appellate court.' That procedure clears the path for future relitigation of the issues between the parties and eliminates a judgment, review of which was prevented through happenstance. When that procedure is followed, the rights of all parties are preserved; none is prejudiced by a decision which in the statutory scheme was only preliminary."

In the case at bar there are no facts which bring the case into the established practice of the Court in dealing with civil cases from a Court in the Federal system which has become moot while on its way to this Court or pending the decision of this Court *on the merits*. There was no question of mootness before the Court of Appeals at the time its order was entered affirming the District Court. As

hereinbefore pointed out, no petition for a writ of certiorari has been applied for by the S. E. C. addressed to the Third Circuit Court of Appeals to review its order affirming the District Court. This decision cannot, therefore, be reviewed by this Court on the merits.

Further, in the case at bar such vacation procedure is not necessary to clear the path in case of future litigation of issues between the debtor and the S. E. C. There are no rights between the parties to the action which are preserved, or which need preserving by such a procedure. The S. E. C. has not shown in its petition for certiorari in any way how or why it will be prejudiced if the decision of the Court of Appeals is permitted to stand. Unlike the situation in *Munsingwear, supra*, the refusal to vacate the judgment here will not hamper the S. E. C. if there is future litigation between the parties here because necessarily there will be an entire new proceeding and a different set of facts if the debtor at any time in the future files a new Chapter XI proceeding for relief under that Section of the Bankruptcy Act.

This is indicated by Section 321 of the Bankruptcy Act, 11 U. S. C. 721 which provides as follows:

> "A debtor may file a petition under this Chapter in a pending bankruptcy proceeding either before or after his adjudication."

The procedure desired by the S.E.C., of having this Court vacate the opinion and judgment of the Court of Appeals, clears no path for future relitigation of the same issues between the parties. Nor would the vacation of the opinion and judgment by this Court preserve the rights of all parties to the proceeding, since there are no rights to be preserved, either past or future. No one is prejudiced by the decision of the Court of Appeals.

C. The fact that the S. E. C. has an opinion on the books not to its liking furnishes no reason for the granting of the writ applied for.

At page 9 of its brief, the S.E.C. states:

> "In the present case, the determination of the court below, if not vacated, may well affect the result of other cases under Chapter XI of the Bankruptcy Act."

We submit that the determination of the Court below and its effect upon the result of other cases under Chapter XI of the Bankruptcy Act, furnishes no valid reason for vacating the decision of the Court of Appeals. We firmly believe that the only reason that the S.E.C. seeks to vacate at this time the opinion and judgment of the Court of Appeals, is because it has an opinion on the books which is not to its liking. This is certainly no reason why this Court should vacate the opinion and judgment of the Court of Appeals. Quite the contrary. An appraisal of the case, we believe, must lead to a denial of the petition of the S.E.C. to review the order of the Court of Appeals entered March 23, 1960.

Conclusion.

For all the foregoing reasons, respondents respectfully urge that the writ of certiorari be denied.

Respectfully submitted,

SAMUEL M. COOMBS, JR.,
Attorney for Receiver,
Respondent.

RAVIN & RAVIN,

By: NATHAN RAVIN, ✓
A Partner,
Attorneys for Lea Fabrics, Inc.,
Respondent.

FURST, FURST & FELDMAN,

By: GEORGE FURST, ✓
A Partner,
Attorneys for Creditors'
Committee, Respondent.

APPENDIX.

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT.

No. 13054.

IN THE MATTER

of

LEA FABRICS, INC.,

Debtor,

vs.

SECURITIES AND EXCHANGE COMMISSION,

Appellant.

APPEAL FROM ORDER OF THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY.

Answer of Lea Fabrics, Inc., Debtor, Unsecured Creditors' Committee, and Receiver of the Debtor, to Petition of Securities and Exchange Commision for Rehearing.

On Wednesday, December 23, 1959, the mandate of this Court would have issued to the United States District Court for the District of New Jersey, as of course, fifteen days having expired after the date of entry of final judgment in the above entitled appeal on December 8, 1959. On that date, December 23, 1959, the Securities and Exchange Commission (S. E. C.) filed its petition for rehearing herein, and the interested parties who are now answering such petition were notified by telephone by Mr. Kiva Berke, of the S. E. C., on that day that such petition was to be filed and that copies of such petition were being mailed special delivery from Washington to all interested parties late in the afternoon of

that date Not having received the copies of the petition for rehearing, counsel for the Receiver called the Clerk of this Court on December 24, 1959, and was advised that such petition had been filed on December 23, 1959. Later in the day, on December 24, 1959, copies of the petition were received by the interested parties now answering said petition.

This Court noted, at page 4 of its opinion, that:

> "Not the least of the considerations which prompt approval of the trial judge's exercise of discretion is the situation of this corporation."

This Court then went on to review the status of the corporation at the time the motion of the S. E. C. was filed to dismiss the Chapter XI proceeding unless the petition therein was amended to comply with the requirements of Chapter X (Sec. 328 of the Bankruptcy Act, 11 U. S. C. A. Sec. 728 (Sup. 1958)). It must be remembered that the S. E. C. filed its motion on the day on which the plan of arrangement under the Chapter XI proceeding was to be approved by the Referee, and upon the day on which the $300,000.00 necessary to effectuate such plan of arrangement was to be deposited with the Receiver by the debtor corporation.

As this Court pointed out at page 3 of its opinion:

> "The plan has been agreed to by the unsecured creditors and the priority creditors, including tax claimants, * * *"

Not only creditors, but stockholders of the corporation are vitally interested in seeing the plan approved by proper order of the Referee, and almost daily are evincing such interest by telephone calls to counsel for all of the interested parties answering this petition for rehearing and the Receiver of the debtor corporation. Every day that such order is delayed the rights of creditors, secured and unsecured, stockholders, and the debtor corporation, under the proposed plan of arrangement, are gravely endangered.

The hearing on the approval of the proposed plan is being adjourned from week to week before the Referee until this appeal is disposed of.

The S. E. C. states, in paragraph 2 of page 1 of its petition:

> "The opinion describes only the formal arrangement to be consummated in the Chapter XI court. It ignores the complicated series of transactions which the debtor had planned to enter into outside the court, including the purchase and sale of various assets and recapitalization of its stock. (See our main brief, pp. 5-6). It may be that this Court made no reference to those transactions because the debtor contended that they had been abandoned."

This is basically the reason given by the S. E. C. why it desires a rehearing. In the final paragraph of its petition, on page 3, the S. E. C. states:

> "• • • we believe to be essentially irrelevant the debtor's contention on this appeal (Brief, p. 5) that 'On confirmation the Debtor's capital structure was and is to remain unchanged. The rights of stockholders will not be changed or impaired.' If this Court is of the view, however, that this *contention, first advanced upon the argument below after the factual record had been completed*, casts some doubt upon our showing that in addition to the Chapter XI arrangement steps will be required to be taken affecting the rights and interests of public stockholders, then it is respectfully suggested that an appropriate course would be to remand the matter to the District Court for further evidence." (Emphasis supplied.)

That the S. E. C. is patently in error in the foregoing statement is borne out by the record below. The decision of this Court is not based upon a contention that was first advanced upon the argument below after the factual record had been completed.

The affidavit of Mr. Fred S. Payne, President of the debtor corporation, in opposition to the motion of the S. E. C. to dismiss, at 32a, is as follows:

> "The cash necessary to pay creditors' claims, is being advanced to the Debtor without any security or strings whatsoever. *On confirmation of the Chapter XI Plan, therefore, the Debtor's capital structure will remain absolutely simple and unchanged. Neither the rights of creditors nor stockholders will be impaired.* (Emphasis supplied.)
>
> "Said Plan bears no relationship to and is not dependent on management's proposals and plans for the Debtor's future, as suggested by the Commission."

The Court below, at pp. 4 and 5 of the hearing before that Court on October 2, 1959, asked questions of and received answers from Mr. Payne and his counsel, Mr. Ravin, relating to the debtor's capital structure and the fact that it would remain unchanged so that neither the rights of creditors nor stockholders would be impaired.

We respectfully submit that this Court should deny the petition of the S. E. C. for a rehearing because this Court's decision is predicated on a proper application of the law to the facts.

Respectfully submitted,

RAVIN & RAVIN,

By: NATHAN RAVIN,
A Partner,
Attorneys for the Debtor.

FURST, FURST & FELDMAN,

By: DAVID E. FELDMAN,
A Partner,
Attorneys for Unsecured Creditors' Committee.

SAMUEL M. COOMBS, JR.,
Attorney for Receiver.

Transcript of Hearing before Referee February 5, 1960 (pages 5 and 6).

"*Direct examination*

"By Mr. Ravin:

"Q. Mr. Fassoulis, what is your interest in Lea Fabrics, Inc.? A. I am the controlling stockholder of a company called Financial Consultants, which is the largest stockholders of Lea Fabrics. In addition to which I have acted as financial adviser to Lea Fabrics.

"Q. Will you tell the Court what the status of your efforts was at the time the appeal was taken from Judge Wortendyke's decision as to raising money to take this case out of court and consummate the plan of arrangement? A. We had a commitment from, a firm commitment for $300,000 which was ready to be deposited to have the company confirmed.

"Q. Yes? A. During the period of that litigation we lost the $300,000 because they looked into another situation.

"Q. You mean you lost the commitment? A. Yes."